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In The

Supreme Court of the United States

October Term 1985

No. 85-169

DAVID L. CHAPMAN, BARBARA E. ROBERTS, DAVID V. EASTON, MICHAEL M. KALUGER, JR., DAVID C. HUNTER, MICHAEL D. FAZIO and CHRISTOPHER L. FAIRCHILD,

Petitioners

-vs-

THE STATE BAR OF CALIFORNIA, CALIFORNIA LEGISLATIVE COUNCIL OF OLDER AMERICANS,

Respondents

On Petition for A Writ Of Certiorari To The California Court of Appeal For The Fourth Appellate District, Division One

RESPONDENT THE STATE BAR OF CALIFORNIA'S BRIEF IN OPPOSITION

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BEST AVAILABLE COPY

QUESTIONS PRESENTED

1. Whether California's Funds for the Provision of Legal Services to Indigent Act, Business and Professions Code, § 6210, et seq., -- which provides that lawyers deposit nominal or short-term client trust funds that are inherently incapable of earning net interest for the client into an aggregated account, from which interest is used to provide legal services to the indigent, and which maintains the obligation of attorneys to deposit client funds, which are not nominal in amount or are not deposited for a short term, into interest-bearing accounts for the benefit of clients -- involves taking of property without just compensation, prohibited by the United States Constitution?

2. Whether there is a reasonable basis in classification and use of client

QUESTIONS PRESENTED
(Cont'd)

funds, which inherently cannot earn interest to benefit the client, for providing funds for legal services to the poor?

3. Whether the statute should be strictly scrutinized because of petitioners' contention that it will cause clients to hesitate to seek services of attorneys?

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No. 85-169

IN THE

SUPREME COURT OF THE UNITED STATES

DAVID L. CHAPMAN, ET AL.

Petitioners,

- vs -

THE STATE BAR OF CALIFORNIA, ET AL.,

Respondents.

RESPONDENT THE STATE BAR OF CALIFORNIA'S BRIEF IN OPPOSITION

Respondent, The State Bar of California (hereinafter "State Bar"), respectfully requests that this Court deny the petition for writ of certiorari seeking review of the opinion in this case of the California Court of Appeal, Fourth Appellate District, following the order of the California Supreme Court summarily denying a petition for hearing. That opinion is reported as Carroll v. State Bar, 166 Cal.App.3d 1193 (1985). (A copy of the opinion is included in petitioner's appendix (hereinafter

"P.A.") to the petition for writ of certiorari. P.A. at 15-50.

STATEMENT OF THE CASE

Petitioners challenge California's Funds For The Provision Of Legal Services To The Indigent Act, Bus. & Prof. Code, § 6210, et seq.,[1] which establishes a program requiring attorneys to deposit nominal and/or short term client trust funds in an aggregated account from which the interest is paid to the State Bar for funding legal services to the indigent by approved non-profit groups. Such programs are generally referred to by the acronym "IOLTA" (Interest on Lawyer Trust Account Program).[2]

California's IOLTA, like other similar programs, specifies that are "nominal" or

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[1]Unless otherwise noted, all references to sections are to California Business and Professions Code.

[2]Thirty-seven states have adopted IOLTAs. California is the largest, having received $19.8 million and allocated $17.2 million as of July 31, 1985.

"short-term" funds are those which are so minimal in amount or are held for such a short time, they inherently cannot generate net interest for the client because any interest earned is dissipated by costs charged by banks and attorneys for administration and accounting . § 6211(a); P.A. at 20-22. California's IOLTA maintains the right and obligation of attorneys to deposit client trust funds, which are capable of earning net interest, into segregated interest-bearing accounts for the benefit of the client. § 6211(b); P.A. at 23. Finally under IOLTA, client trust funds on deposit remain available, on demand, and the client's rights to withdraw, obligate or convey them are unaffected.

This matter below was originally a coordinated proceeding involving two cases, Carroll v. State Bar (Superior Court of San Diego County, No. N22139) and Seuthe, et al. v. State Bar (Superior Court of Los

Angeles County, No. C455587). Plaintiff in Carroll was a client and the legal secretary for the attorney representing her; all plaintiffs in Seuthe, et al., are attorneys. Seuthe, et al. was brought as a class action, but the class was never certified, and petitioners appear only in their individual capacities.

The opinion below reverses a trial court judgment misconstruing IOLTA as client-voluntary in that § 6211(b) permits attorneys to deposit nominal and short-term trust funds into interest-bearing accounts, for charitable purposes other than those authorized by IOLTA. The court of appeal held that § 6211(a), is plain, clear, and unambiguous, requiring mandatory deposits

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[3]The court also found that the legislative history showed a mandatory program was adopted to eliminate the tax consequences and problems of "assigned income" that a client-voluntary IOLTA would create. The legislature was aware that under Revenue (Continued)

of nominal and short-term client trust funds into IOLTA accounts,[3] and that § 6211(b) permits investing of those client funds not nominal or short term and thus capable of earning net interest. P.A. at 22, 23. The court then ruled the statute is not unconstitutionally vague and ambiguous,[4] and does not involve the uncompensated taking of property prohibited by U.S. Constitution, Fifth Amendment. It rejected petitioners' equal protection claim, holding that instead there is a rational relationship between the method employed and goal of IOLTA, and finding no merit to the contention that the statute infringed on

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[3](Continued) Ruling 81-209, 1981-12 C.B.16 a client-voluntary IOLTA would engender debilitating costs of accounting for tax purposes. P.A. at 27-32.

[4]Petitioners do not seek review of this issue.

the right to counsel and thus should be subject to strict scrutiny.

After the decision of the court of appeal, only the attorney-plaintiffs in Seuthe, et al., filed a petition for hearing in the California Supreme Court; the sole client-plaintiff, Mrs. Carroll, did not seek further review. The petition for hearing was denied without opinion. The attorney-plaintiffs in this case, rev'd sub nom. Chapman, et al., v. State Bar, now petition for a writ of certiorari in this Court.

REASONS WHY THE WRIT SHOULD BE DENIED

The opinion below presents no important federal questions involving taking of clients' property without just compensation, any unreasonable classification, or impairment of any fundamental right. In addition, the opinion below is not in conflict with any decisions of other jurisdictions.

A. The Opinion Below Was Decided In A Way Consistent With The Applicable Decisions Of This Court And Presents No Important Questions Of Federal Law Which Have Not Been Settled By This Court

1. The Taking Of Property Issue. The court below correctly held that IOLTA involves no taking of property without just compensation, prohibited by the Fifth Amendment. In determining whether there is such a constitutional violation, this Court has utilized a multifactor balancing test which considers: (1) economic impact, (2) any interference with reasonable investment back expectations, and (3) the character of the governmental actions. Ruckelhaus v. Monsanto Co., ___ U.S. ___, 81 L.Ed.2d 815, 104 S.Ct. 2862, 2875 (1984); Pruneyard Shopping Center v. Robins 447 U.S. 74, 83 (1980); Penn Central Transportation Co. v. New York City 438 U.S. 104, 124 (1978). These factors were judiciously applied in the opinion below. P.A. at 36-42.

(a) No Economic Impact Nor Reasonable Investment-Backed Expectation. The court of appeal correctly found that IOLTA has no economic impact on clients. Id. Deposits into IOLTA accounts are limited only to those client funds which under current banking regulations are inherently incapable of earning net interest for the client in other interest-bearing accounts. Before the enactment of IOLTA, attorneys would deposit such funds into a single, aggregate non-interest account to carry out their ethical obligation of securing client funds. ABA Comm. on Ethics and Prof. Resp. Formal Op. No. 348, 68 ABA 1502. These nominal and short-term funds were not deposited in interest accounts because service fees charged by banks or handling costs by attorneys would exceed any interest earned. P.A. at 39. IOLTA is able to generate net income only by avoiding these transactional costs through

the payment of the interest to a single beneficiary designated by statute.

Petitioners suggest without explanation that some profit can be obtained by clients from the aggregated IOLTA accounts. They suggest value may be realized if a client were allowed to control the disposition of interest earned on the nominal or short-term funds by designating the recipient of the interest as himself or some charity. This is the same client-voluntary argument rejected below. No net interest is possible if a client participates. With any degree of client control, the interest will be treated as taxable "assigned income." P.A. at 27-28; see Helvering v. Horst, 311 U.S. 112 (1940); Lucas v. Earl, 281 U.S. 111 (1930); Rev. Ruling 81-209, 1981-12 C.B.16. To determine the amount remittable to each client and to meet reporting and other tax consequences, each client's share of the interest must be calculated and accounted

for, thereby engendering the debilitating administrative costs IOLTA is designed to eliminate.

In sum, funds which before IOLTA could not earn interest for the client are still incapable of earning interest; and funds which before could earn interest must still be invested on behalf of the client. The client's economic stake is unaffected by IOLTA[5] The court below correctly concluded no client is stripped of earnings and no person has suffered any economic

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[5]The only significant change made by IOLTA is that financial institutions, which previously enjoyed the "free" use of the nominal and short-term funds held in client trust accounts, must now pay interest to the State Bar for distribution for the legal services to the poor.

loss. P.A. at 38. Accordingly, IOLTA has not, and by definition cannot, interfere with any client's "distinct investment-backed expectations." Id. at 39, 40. Any claim on the monetary value of such interest is no more than a unilateral expectation. As the court below concluded:

> "To have a property interest subject to protection under the Fifth Amendment, one must have more than an abstract need or desire, more than unilateral expectations." Id., citing Board of Regents v. Roth 408 U.S. 564, 577 (1972); see also Perry v. Sindermann 408 U.S. 593, 601 (1972).

The failure of petitioners' taking argument is apparent in their inability to state what appropriate compensation is due. After all, it is only the state's failure to provide for just compensation which renders some action invalid as violative of the Fifth Amendment's mandate. See Texaco v. Short 454 U.S. 516, 530 (1982).

Petitioners misunderstand this principle of just compensation when they

claim that the rights they assert should not be tied to a dollars and cents analysis. Petition, p. 20.

Just compensation must be measured by loss to the owner. See United States v. Twin City Power Co., 350 U.S. 222, 228 (1956) ("since the owner is to receive no more than indemnity for his loss, his award cannot be enhanced by any gain to the taker"); Monongahela Navigation Co. v. United States, 148 U.S. 312 (1983) (standard is to provide "a full and just equivalent"). By definition, funds deposited in IOLTA accounts are those with no interest-earning potential to the client. Since no interest potential has been lost, and the trust account corpus is not touched, the detriment to the owner--what the client has lost--is zero. Holders of nominal or short-term accounts are already in as good a position pecuniarily as they would be absent the alleged taking. IOLTA has deprived them of

nothing, and there is nothing to restore to them. By definition there could not have been a deprivation of a valuable property interest in violation of the Fifth Amendment.

(b) Character of IOLTA: Economic Regulation For Public Good. The court below correctly concluded that IOLTA promotes the common good without diminishing a client's economic interest. P.A. at 41, 42. It properly applied the standards promulgated by this Court: when no physical invasion of property is involved, a "taking" will be tested by examining the adjustments of economic burdens and benefits, on the one hand, against the public purpose served, on the other. Penn Central Transportation Co. v. New York City 438 U.S. at 142, 125; Loretto v. Teleprompter, 458 U.S. 419, 426 (1982). "Where the public good is great, and a 'taking' is minimal, [the action] is permissible." P.A. at 42.

Thus, this Court has generally upheld substantial restrictions on private property use when significant public policy goals are involved. In Andrus v. Allard, 444 U.S. 51, 65 (1979), this Court upheld a prohibition on the sale or possession of migratory birds and their parts even though "this adjustment curtails some potential for the use or economic exploitation of property." In Euclid v. Ambler Realty Co. 272 U.S. 365 (1926), this court held that the need to control commercial development justified a restriction which diminished the potential value of private land by 75%. In Hadacheck v. Sebastion, 239 U.S. 394 (1915), elimination of a brickyard operation in a residential area was upheld although property value diminished 87%. In William C. Hass & Co. v. City and County of San Francisco, 605 F.2d 1117, 1120 (9th. Cir. 1979), the court held open space development

considerations justified restriction which diminished property value by 95%.

The nature of the effect on private rights under IOLTA contrasts sharply with the private rights effected in these cases. As stated above, a client's economic interest is unchanged by IOLTA. In short, a significant and urgent public need is met without any significant consequences or restrictions on private property. As this Court concluded in an analogous context,

> The State surely has the power to condition the ownership of private property on compliance with conditions that impose such a slight burden on the owner while providing such clear benefits to the State. Texaco v. Short, 454 U.S. at 530.

Throughout the proceedings petitioners have not disputed the legitimacy of IOLTA to provide civil legal services to the poor. Petition, p. 12. Their objection is that IOLTA allegedly removes all beneficial uses of nominal and short-term client funds. Petition, p. 20.

As stated above, IOLTA accounts apply only to client trust funds which cannot benefit clients. This principle aside, petitioners' argument is still flawed because of its too-narrow focus on use of nominal and short term funds. The government regulatory impact must be judged against the property's value as a whole, not against its impact on any part or particular use. Andrus v. Allard, 444 U.S. 51, 65-66.

For example, in Penn Central, supra, plaintiffs argued that the airspace above an existing building was a valuable property right, that the city's refusal to let them build an additional structure totally deprived them of all gainful use of that space, and that therefore their right to the airspace had been "taken" regardless of the significance of any public interest involved.

This Court held that the restriction's impact must be judged against

the whole parcel's value, including that of the existing building, not just that of the air rights segment:

> "Taking" jurisprudence does not divide a single parcel into discrete segments and attempt to determine whether rights in a particular segment have been entirely abrogated. In deciding whether particular governmental action has effected a taking, this Court focuses rather both on the character of the action and on the nature and extent of the interference with rights in the parcel as a whole - here, the city tax block designated as the "landmark site." Penn Central, supra, 438 U.S. at 130 (emp. added).

Since the site and the existing building retained some economic value despite the limitation on additional development, the Court found no taking.

Similarly, IOLTA's impact on a client's trust fund must be assessed against his whole property interest. IOLTA leaves unaffected the rights of clients to have invested trust funds, which are not nominal or short term. As for nominal and short-

term funds, the principal remains available on demand, and the client's rights to withdraw, obligate or convey it are unaffected by IOLTA. Even if some theoretical right to exclusive control of property is effected, the impact of a client's total rights would not be substantial enough to warrant the finding of a "taking." This Court has stated:

> [T]he denial of one traditional property right does not always amount to a taking. At least where an owner possesses a full "bundle" of property rights, the destruction of one "strand" of the bundle is not a taking, because the aggregate must be viewed in its entirety. Andrus v. Allard, 444 U.S. at 65-66 (emp. added).

(c) Petitioners Misapply the Webb's Case. Throughout the proceedings, petitioners have relied principally on one decision of this Court, Webb's Fabulous Pharmacies, Inc. v. Beckwith, 449 U.S. 155 (1980).

Although Webb's is facially similar to the case at bar in that both concern interest earned on deposited funds, the court below properly noted that Webb's failed to address the issues pertinent to this case. P.A. at 41. In Webb's, the purchaser of Webb's Fabulous Pharmacies interpleaded the purchase price and named as defendants both Webb's and its creditors. The buyer deposited over $1,800,000, with the court. One Florida statute exacted a fee for the clerk's services, amounting in this case to $9,228.74. The $1.8 million remained on deposit until it was delivered to Webb's' receiver over a year later. By then the interpleader fund had earned over $90,000 in interest. Under a second Florida statute, this interest was deemed income of the county. This Court held that there was no justification shown for the state's retention of the interest. Webb's, at 163. It specifically rejected the state's

argument that the withholding was justified as a cost reasonably related to the use of the courts, which was already satisfied by the substantial fee prescribed by the first statute. This Court noted that Florida's statute would allow the state to exact two tolls on the interpleader fund. Id., at 160. The Court carefully emphasized its holding was restricted to this type of "double-charge" situation:

> We hold that under the narrow circumstances of this case - where there is a separate and distinct state statute authorizing a clerk's fee for services rendered based upon the amount of principal deposit; where the deposited fund intself concededly is private; and where the deposit in the court's registry is required by state statute in order for the deposit to avail itself of the statutory protection from claim of creditors and others - Seminole County's taking unto itself ... the interest earned on the interpleader fund while it was in the registry of the court was a taking violative of the Fifth and Fourteenth Amendments. We express no view as to the constitutionality of a statute that prescribes the county's retention of interest earned, where the interest would be the only return to the county for the services it renders. 449 U.S. at 165.

In IOLTA, no such inequitable double charge exists.

In addition, Webb's is factually dissimilar on other grounds. Most significantly, the disputed interest on the fund in Webb's was clearly a property interest. The amount involved ($1,800,000), the interest earned (over $90,000), and the time of deposit (over a year), indicate that the fund in Webb's was neither nominal nor short term, and that the interest due each creditor could have been easily calculated. See P.A. at 410. By contrast, § 6211(a) applies only to normal or short term funds, on which clients cannot earn interest. Moreover, § 6211(b) expressly provides for deposit of client funds into interest bearing accounts for the client's benefit where the sum deposited or the time which it will be held is substantial (like the Webb's situation). See also, Matter of Interest on Trust Accounts 402 So.2d 389,

395, 396 and Matter of the Adoption of Amendments to CPR DR-102 IOLTA, slip op. pp. 6, 8, 9 (Supreme Court of Washington, June 19, 1984). Moreover, this Court also noted in Webb's that the statute could have been justified if it promoted the general welfare, but that the Florida statute suggested no reasonable basis for the taking of the interest of the interpleader fund. Webb's, supra, at 163. By contrast, the California Legislature has expressly found that IOLTA "will aid in the advancement of the science of jurisprudence and the improvement of the administration of justice." § 6210. Moreover, petitioners concede that the purposes of IOLTA are important to the common good. Petition, p. 12. The court below, after carefully balancing the benefits and burdens, found IOLTA to further public policy without diminishing client's rights. P.A. at 41-42.

Petitioners have relied on language in Webb's holding that "the State's having mandated the accrual of interest does not mean the State or its designate is entitled to assume ownership of the interest," and rejecting Florida's argument that "the statute takes only what it creates." 449 U.S. at 162, 163. Out of context, this dictum appears to bolster petitioners' allegation of a taking by IOLTA. However, this language is inapplicable to the differing factual circumstances of IOLTA.

As stated above, the fund in Webb's was always capable of earning interest. However, when deposited in interpleader, state law originally did not obligate the court clerk to invest the fund in an interest-bearing account. Therefore, the Florida statute which commanded that such funds be placed in an interest-bearing account, merely restored the fund's interest-earning potential which was lost

under the interpleader statute. The fact that this state statute restored the potential did not alter the continued private nature of the property right in such interest.

The critical distinction is that in IOLTA, the funds subject to the statute are inherently not capable of earning interest in private hands. The client, no matter what he does with his individual fund, can never earn net interest on his nominal or short-term trust account. This intrinsic character, not some state statute, deprives the funds of any interest-bearing potential. IOLTA, by aggregating such funds and mandating payment of interest without subaccounting, truly has "created" something where nothing existed before. No private property right or expectation ever existed in such interest. In Webb's on the other hand, the state statute did not "create" interest potential where none inherently existed, it

simply removed the artificial barrier to that potential put up by another state restriction. See Matter of Interest on Trust Accounts, 402 So.2d at 395; Petition of Minn. Bar, 332 N.W.2d 252, 157 (Minn. 1982); Petition of New Hampshire Bar, 453 A.2d 1258, 1261 (N.H. 1982).[6]

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[6]In First Nat'l. Bank & Trust Co. of Evanston v. Rosewell, 93 Ill.3d 388 (1982), 444 N.E.2d 126, cert. denied, 464 U.S. 803 (1983), the Illinois Supreme Court considered a taxpayer's contention that failure to pay interest on taxes paid under protest and later refunded constituted a taking in violation of the Fifth Amendment. The taxpayer, citing Webb's, argued that if he were compelled to deposit the funds with the state he was entitled to the interest generated by such moneys, not the state. The amount involved exceeded $1 million so that interest was of significance.

The court concluded that Webb's did not establish any per se rule concerning property rights to interest on deposited money. Rather the focus on Webb's was on the inequity of withholding interest and assessing a service charge as well, and the Webb's Court expressed no view as to constitutionality of interest retention absent such double billing. The Illinois court reasoned that since the Illinois statute had no such service fee, "we view the retention of accrued interest as not constitutionally prohibited." 93 Ill.2d at 395.

2. Equal Protection

(a) Rational Basis. Petitioners contend that IOLTA unlawfully discriminates between clients who have nominal and short-term funds on deposit with attorneys and those who do not. If a classification has some reasonable basis, it does not offend the Constitution simply because some inequality may result; statutory discrimination will not be set aside if any state of facts reasonably may be conceived to justify it. Dandridge v. Williams, 397 U.S. 485 (1970). In this case, the court below correctly applied this standard in finding there is a rational basis for the use of funds, which cannot result in any net gain or loss to the client to provide funds, for legal services to the poor. P.A. at 46.[7]

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[7]See also Cohan v. Alvord 162 Cal.App.3d 176 (1984), where plaintiffs alleged that a statute that provides for the payment of interest on refunded property taxes only (Continued)

(b) No Strict Scrutiny: No Denial Of Right To Counsel. Petitioners contend that IOLTA impinges on the right to counsel, which they state, without the benefit of any authority, is a fundamental right, and thus is subject to the strict scrutiny test. The court below correctly rejected this unsupported argument that clients who seek the services of lawyers would now hesitate to do so because of IOLTA. P.A., at 47-49.[8] .

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[7](Continued) when the interest is $10 or more violated equal protection. The court held "... the de minimis $10 classification scheme ... is reasonably related to the legitimate state interest of easing administrative burdens and is not violative of the right to equal protection under either federal or state law...."

[8]The record below, Appellant's Appendix In Lieu of Clerk's Transcript, at 901-905, showed, for example, that among the IOLTA accounts of the attorney-petitioners in this case, only one account was generating net interest for the period May-August 1983. That account of petitioner David V. Easton aggregated net interest of 37 cents. An argument that (Continued)

This court has rejected similar constitutional challenges that court costs and fees (which will usually constitute nominal and short-term client trust funds under IOLTA if advanced to the attorney) deny access to the courts. See, e.g., United States v. Kras, 409 U.S. 436 (1973); Ortwein v. Schwab, 410 U.S. 656 (1973). This Court has reasoned that payment of fees and costs may subject some litigants to inconvenience, but such inconvenience does not rise to a "'fundamental interest that is gained or lost'" because of the effect of the imposition of a fee. Accordingly, such matters have been analyzed and sustained by the rational basis test. Id., 660.

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[8](Continued) clients would forego the services of Mr. Easton because they could not claim their respective share of the 37 cents is not credible.

B. The Opinion Below Is Not In Conflict With The Decisions Of Another State Court Or Of A Federal Court Of Appeals.

Petitioners assert jurisdiction of this Court under Rule 17.1(b), suggesting that the opinion of the court below is in conflict with other state courts that have reviewed or adopted IOLTA or with a decision of a federal court of appeals. Petitioners make this assertion without any citations or analysis. The Brief of Amici Curiae In Opposition To Granting Of A Writ Of Certiorari, pp. 5-7, correctly sets forth the status of the opinions of the courts in other jurisdictions, and we adopt their position herein. As demonstrated by amici curiae, the opinion below is not in conflict with other state courts or with any decision of a federal court of appeals. Any suggestion of conflict by petitioners is misleading and should be rejected.

CONCLUSION

For all of the foregoing reasons, the petiton for writ of certiorari should be denied.

Respectfully submitted,

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CERTIFICATE OF SERVICE

The undersigned, a member of the bar of the Supreme Court of the United States, certifies that three copies of the RESPONDENT STATE BAR OF CALIFORNIA'S BRIEF IN OPPOSITION have been served on counsels of record for the parties herein by mailing same, first-class postage prepaid, this the 30th day of August 1985, as follows:

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ALL PARTIES REQUIRED TO BE SERVED HAVE BEEN SERVED.

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In addition to the above persons, the following have also been served in the same manner as above:

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(Cont'd)

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Fourth Appellate District
Room 6010, 1350 Front Street
San Diego, CA 92101

Robert D. Zumwalt, Clerk
Superior Court of San Diego County
County Courthouse
220 West Broadway
San Diego, CA 92101
(For: Hon. F. V. Lopardo)

Judicial Council
350 McAllister, Room 3154
San Francisco, CA 94102

Herbert M. Rosenthal

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